

## FACILITATING PRIVATE FINANCING OF PASSENGER VESSELS

JUNE 26, 1956.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. BONNER, from the Committee on Merchant Marine and Fisheries, submitted the following

### REPORT

[To accompany H. R. 11554]

The Committee on Merchant Marine and Fisheries, to whom was referred the bill (H. R. 11554) to amend certain provisions of title XI of the Merchant Marine Act, 1936, as amended, to facilitate private financing of passenger vessels in the interest of national defense, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

That title XI of the Merchant Marine Act, 1936, as amended (46 U. S. C. 1271-1279), is amended as follows:

(a) Sections 1101 (f) and 1103 (a) and (b), are amended by striking out the words "90 per centum of" wherever those words appear in such sections.

(b) Section 1101 (f) is amended by striking out of the proviso the words "except for certain special purpose vessels as provided for in subsections (a) and (b) of section 1103 (46 U. S. C. 1273)" and the commas which immediately precede and follow those words.

(c) Section 1103 (a) and (b) are amended by striking out the provisos.

(d) Section 1103 (d) is amended to read as follows: "(d) The faith of the United States is solemnly pledged to the payment of interest on and the unpaid balance of each mortgage and loan insured under this title."

(e) Section 1105 (a) (1) and (a) (2) are amended by striking out the words "the insured portion of" wherever such words appear in those sections.

(f) The last sentence of section 1105 (c) (1) is amended to read as follows: "In the event the Secretary of Commerce shall receive through the sale of the vessel an amount of cash in excess of any payment made to the mortgagee under subsection (a) (1) of this section, and the expenses of collection of such amount, he shall pay such excess to the borrower."

(g) The last sentence of section 1105 (c) (2) is amended to read as follows: "In the event the Secretary of Commerce shall receive through the sale of the property

an amount of cash in excess of any payment made to the lender under subsection (a) (2) of this section and the expenses of collection of such amount, he shall pay such excess to the borrower."

The purpose of this bill is to amend certain provisions of title XI of the Merchant Marine Act of 1936, as amended, to facilitate the private financing of new merchant ship construction. Under existing law ship construction or reconstruction may be financed by direct Government loans, secured by first preferred ship mortgages, covering not more than 75 percent of the purchase price on vessels on which construction subsidy is allowed, and not more than 87½ percent of vessels on which no construction subsidy is allowed. In addition, Public Law 781, 83d Congress, 2d session, amended the 1936 act to authorize the Government to insure the interest on and 90 percent of the unpaid principal of privately financed loans and mortgages on vessels, except that in the case of "special purpose" vessels the insurance may cover the interest and 100 percent of the unpaid principal. Under this law the requirements for cash down payment of at least 25 percent of the construction or reconstruction cost of a vessel under construction subsidy, and at least 12½ percent of the construction or reconstruction cost of other vessels of approved size and speed, are the same as provided in the case of construction loans made directly by the Government.

This bill would amend the mortgage insurance provisions of the 1936 act so as to authorize 100 percent insurance of the interest and the unpaid principal of all ship loans and mortgages covering the construction and conversion of vessels needed in the American merchant marine to carry out the national maritime policy as declared in the Merchant Marine Act of 1936. Thus, the present limitation of 100 percent mortgage insurance applicable to so-called special-purpose vessels would be removed and the authority would be extended to construction and reconstruction projects for all types of ships required in the national interest.

#### BACKGROUND OF THE LEGISLATION

Title XI of the Merchant Marine Act of 1936 was added in 1938, but eligibility for insurance thereunder was confined to operators who would construct new vessels for use only in (a) domestic trade, (b) foreign trade between the United States and foreign countries in continental North America, including nearby islands, or (c) in the fishing trade or industry. The bill was extremely limited in its scope, and only a negligible number of contracts of mortgage insurance, covering financing totaling less than \$6 million, were entered into between 1938 and 1953.

In 1953 an attempt was made to broaden the scope and effectiveness of the Federal ship mortgage insurance law, with the objective to obtain more private financing of necessary new ship construction. The 1953 amendments made a number of improvements, but departed from the 100 percent mortgage insurance of the original law by limiting the Government's insurance to only 90 percent of the mortgage or loan. They also provided that the Government could not provide insurance unless the Secretary of Commerce found that the interest rate of the loan or mortgage was less than the going interest rate for uninsured ship construction loans of similar character. The act

proved to be a total failure, and new amendments were introduced the following year, removing the features which financing institutions had found objectionable in the previous legislation, and providing for 100 percent insurance. Extensive hearings were held on the 1954 amendments. All witnesses representing private financing institutions, the shipping industry, and the Department of Commerce testified strongly to the effect that if private financing were to be available, it was necessary that the Government insurance should be increased from 90 percent of the loan to 100 percent. The General Accounting Office, while not objecting to that aspect of the bill, questioned whether the increase was necessary to accomplish its purpose. The bill, as enacted, retained the 90 percent limitation, except in the case of special purpose vessels, in the hope that its provisions were sufficiently attractive to induce private financial interests not only to provide the use of private capital, but to assume a portion of the risk.

#### HEARINGS ON THE BILL

In hearings on this bill, however, the General Accounting Office concluded that experience under Public Law 781, the 1954 amendments, has shown that the intent of the statute, insofar as it contemplated an assumption of risk by lending institutions of the uninsured portions of ship mortgages, is not being realized. In practice the lending institutions have refused to make loans or accept ship mortgages without cash collateral to cover the uninsured 10 percent of the mortgage. In fact, the reluctance of lending institutions to assume any portion of the risk of the uninsured portions of mortgages and loans works a hardship on the mortgagors, which was not intended by the present statute.

At the same time, the Secretary of Commerce is unwilling to depart from his desired policy of denying recourse to the available authority to provide direct Government loans under the 1936 act, but insists upon the financing of new ship construction through private sources.

This bill, as introduced, simply provided for extending 100 percent mortgage insurance to cover construction loans on passenger vessels. Today our merchant marine is more seriously unbalanced in the category of passenger ships than in any other of the types that are essential in time of national emergency. The highest defense authorities have repeatedly advised that, because of its potential for troop transport, the national security demands an adequate, modern passenger ship component in our active oceangoing merchant fleet. Such ships are expensive, complicated, and take a long time to create by either new construction or conversion. Yet, they are needed immediately in the event of emergency.

Only three new passenger ships have found their way into the privately owned merchant marine since World War II. And, through World War losses and obsolescence, there are now only 39 active passenger vessels under the American flag, as against 123 in operation in 1939 at the outbreak of World War II. Some contracts have recently been entered into for the replacement of some of the existing passenger fleet. And one new operator has applied for construction and operating subsidy under the terms of the Merchant Marine Act of 1936, to establish a new one-class passenger service across the North Atlantic on an essential trade route not presently served by any American-flag passenger ships.

Of a commercial fleet which includes as many as 45 ships to north Europe alone, just 2 fly the American flag, and 1 of them has reached an age requiring early replacement. In 1954 we carried only 18 percent of the total north Europe passenger movement. At the present time the tourist class passengers represent 50 percent of the total movement in the North Atlantic. In 1954 there were 250,000 tourist accommodations sold, of a total of somewhat less than 500,000 of all classes moving between New York and north Europe. Even more significant is the fact that between 1951 and 1954, practically the entire increase in traffic has been in the tourist class, which has grown by 136 percent in that very short time. 157,000 tourist class passengers moved in 1951, as compared with 371,000 in 1954. Corresponding advances were made in 1955. Thus, it is obvious that not only the needs of national defense, but the needs of American commerce will be served by expansion of our passenger-carrying fleet, particularly in the field of development of modern competitive tourist class vessels.

In hearings held on the bill the Maritime Administrator supported its objective and called attention to the special problems involved in fostering the development of an adequate passenger ship component in the merchant marine. He said that passenger vessels required some special treatment because of—

\* \* \* the very heavy capital investment required to purchase such vessels, the relative unadaptability of such vessels to trades other than those for which they are designed, and the heavy investment risk relative to prospective earnings. The money invested in a passenger vessel, which is relatively unadaptable to trades other than the trade for which it is designed, would buy a number of cargo vessels which are relatively more adaptable to other trades. In the case of passenger vessels the risk is greater relative to earnings and less widely spread than in the case of cargo vessels. Passenger vessels are essential to national defense. On the basis of Department of Defense requirements for passenger vessels immediately upon mobilization, our merchant fleet is now substantially deficient in such vessels.

In a memorandum prepared by a joint Maritime Administration-Navy group, transmitted by letter of May 22, 1956, from the Assistant Secretary of the Navy to the chairman of your committee, it was stated that from the standpoint of initial mobilization requirements, the Joint Chiefs of Staff estimate that there is today a deficiency of 15 large passenger vessels in the active merchant marine. Substantial deficiencies likewise exist in other categories of vessels.

The Maritime Administrator urged that the bill be amended so as to provide for 100 percent mortgage insurance on all ship construction loans and mortgages which are eligible for insurance. He stated:

The downpayment required by title XI for a mortgage to be eligible for insurance is 25 percent of the cost to the purchaser if the vessel is built with construction subsidy, and 12½ percent of such cost if the vessel is built without construction subsidy. This is the same downpayment as is required under title V when the United States accepts a mortgage as part of the payment for a vessel. The practical effect of only 90 percent insurance of mortgages on passenger vessels is to



increase the downpayment required, since lenders require collateral to secure the uninsured portion, and to make the transaction not a nonrecourse transaction with respect to the uninsured portion of the mortgage.

The practical result of 90 percent insurance of mortgages in increasing the downpayment required applies to all vessels to which 90 percent insurance applies, because lenders require collateral to secure the uninsured portion of the mortgage.

In the Review of Maritime Subsidy Policy, issued by the Maritime Administration and the Department of Commerce on May 3, 1954, it is recommended (p. 99) that the Department of Commerce request amendments to title XI which would authorize 100 percent insurance of the unpaid principal of all ship loans and mortgages.

When questioned as to the amendments proposed by the Maritime Administrator, the General Accounting Office witness testified that they were reasonable and consistent with the objectives of the bill, and justified by experience under existing law.

The Department of the Navy, in reporting on the bill on behalf of the Department of Defense, favored its enactment. The report states:

It is believed that this bill may provide some stimulus to the construction of passenger vessels, thereby furthering the Maritime Administration's long-range program for replacement of our country's passenger fleet. The present shipbuilding industry is badly in need of additional work and, for this reason, it is considered that the special benefit which would be accorded private operators by this bill is justified. It is considered that passenger vessels with troop-carrying potentialities are of equal or greater defense value than many special-purpose vessels in time of war. If the benefit of 100-percent insurance on the principal and interest of a mortgage or loan is to be granted for special-purpose vessels, it seems reasonable that it should also be granted for passenger vessels for carrying troops.

In view of all the circumstances, your committee believes that this is highly desirable legislation, and is particularly necessary at this time in order to encourage expansion of the merchant marine where needed, and to avoid the sterilization of private capital which would otherwise be available for new ship construction, but for the requirement of financing institutions of cash collateralization of the uninsured 10 percent, under the existing law. The bill, as so amended, will make the mortgage insurance law consistent with the existing provisions of law providing for Government financing. Thus, it is the belief of the committee that the purposes of the Merchant Marine Act of 1936 might be accomplished through the use of private capital, secured by Federal mortgage insurance, thus obviating heavy appropriations necessary when Government financing is employed.

The history of experience in Government financing of ship construction under the Merchant Marine Act of 1936 shows that there has never been a default or loss to the Government.

The departmental reports are as follows:

## COMPTROLLER GENERAL OF THE UNITED STATES,

*Washington, June 25, 1956.*

HON. HERBERT C. BONNER,

*Chairman, Committee on Merchant Marine and Fisheries,  
House of Representatives.*

DEAR MR. CHAIRMAN: This letter is in response to the informal request of Mr. John M. Drewry, chief counsel of your committee, to Mr. Graydon L. Andrews of our office, who testified on June 20, 1956, relative to H. R. 11554, 84th Congress.

H. R. 11554 proposed to amend sections 1103 (a) and 1103 (b) of title XI of the Merchant Marine Act, 1936, as amended, to authorize the Secretary of Commerce to insure 100 percent of the principal of and interest on mortgages or construction loans on passenger vessels. At present, the Secretary is authorized to insure 100 percent of the principal of and interest on mortgages and loans on "special purpose" vessels, and 100 percent of the interest on but only 90 percent of the principal of mortgages and loans on other vessels.

In our prepared statement which was delivered during the hearing before your committee on June 30, we stated that the present 90 percent limitation apparently has not had the effect it contemplated, namely, to have the mortgagee assume a portion of the risk. Instead, the mortgagees are requiring collateral or guaranty by acceptable outside parties to cover the uninsured 10 percent of the agreed mortgages. In addition to the instances cited in our prepared statement, we had been advised that, even in connection with the construction of tankers under Public Law 575, 83d Congress, under which revenues for 10 years are assured by charter contracts with the Government, the lending institutions are requiring collateral or guaranties to cover the uninsured 10 percent of the mortgages. For these reasons, together with the fact that Congress previously had recognized the need for special consideration to passenger vessels, we see no objection to H. R. 11554.

At the hearing, the Maritime Administrator reported that the practical effect of the 90 percent limitation (based upon nearly 3 years experience under Public Law 288, 83d Cong.) is to increase the down payment required of the mortgagors on all vessels subject to that limitation. Accordingly, the Maritime Administration proposed an amendment to H. R. 11554 which would extend 100 percent Government mortgage insurance coverage to all vessels.

In view of (1) the facts now developed as to the failure of the 90 percent limitation to accomplish its contemplated result, (2) the fact that the proposed amendment would not require any greater risk by the Government than has been accepted under title V since the enactment of the Merchant Marine Act of 1936, and (3) the fact that increased down payments by the mortgagors may well be an unintended deterrent to the ship construction program, we offer no objection to the favorable consideration of H. R. 11554 as introduced nor to the amendment thereto proposed by the Maritime Administration.

Sincerely yours,

JOSEPH CAMPBELL,  
*Comptroller General of the United States.*

DEPARTMENT OF THE NAVY,  
OFFICE OF THE SECRETARY,  
Washington, D. C., June 21, 1956.

HON. HERBERT C. BONNER,  
*Chairman, Committee on Merchant Marine and Fisheries,  
House of Representatives, Washington, D. C.*

MY DEAR MR. CHAIRMAN: Your request for comment on H. R. 11554, a bill to amend certain provisions of title XI of the Merchant Marine Act, 1936, as amended, to facilitate private financing of passenger vessels in the interest of national defense, and for other purposes, has been assigned to this Department by the Secretary of Defense for the preparation of a report thereon expressing the views of the Department of Defense.

H. R. 11554 would amend sections 1103 (a) and (b) of the Merchant Marine Act, 1936, as amended to provide that in the case of passenger vessels having the characteristics set forth in title V of the act, in addition to special purpose vessels essential to national defense, the Secretary of Commerce may insure 100 percent of the principal and interest for any mortgage or loan eligible for insurance provided in the act.

It is believed that this bill may provide some stimulus to the construction of passenger vessels, thereby furthering the Maritime Administration's long-range program for replacement of our country's passenger fleet. The present shipbuilding industry is badly in need of additional work and, for this reason, it is considered that the special benefit which would be accorded private operators by this bill is justified. It is considered that passenger vessels with troop-carrying potentialities are of equal or greater defense value than many special purpose vessels in time of war. If the benefit of 100 percent insurance on the principal and interest of a mortgage or loan is to be granted for special purpose vessels, it seems reasonable that it should also be granted for passenger vessels for carrying troops.

Accordingly, the Department of the Navy, on behalf of the Department of Defense, favors enactment of H. R. 11554. However, it should be made clear that the important policy decision regarding whether any pledge of the faith and credit of the United States to cover insurance on passenger vessels would be in the overall national interest is not within the purview of the Department of Defense.

This report has been coordinated within the Department of Defense in accordance with procedures prescribed by the Secretary of Defense.

There has been insufficient time to obtain advice from the Bureau of the Budget as to the relationship of this report on H. R. 11554 to the program of the President.

Sincerely yours,

N. J. FRANK, Jr.,  
*Captain, United States Navy,  
Acting Director, Office of Legislative Liaison  
(For the Secretary of the Navy.)*

#### CHANGES IN EXISTING LAW

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as introduced, are shown as follows (existing law proposed to be omitted is

enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

MERCHANT MARINE ACT, 1936

SEC. 1103. (a) The Secretary of Commerce, upon application by the mortgagor, is authorized to insure as hereinafter provided the interest on and 90 per centum of the unpaid balance of the principal of, any mortgage offered to him which is eligible for insurance as hereinafter provided and, upon such terms as the Secretary of Commerce may prescribe, is authorized to make commitments to insure any such mortgage prior to the date of execution or disbursement thereon: *Provided*, That in the case of special purpose vessels certified by the Secretary of Defense to be essential to national defense, *and in the case of passenger vessels having the tonnage, speed, passenger accommodations, and other characteristics set forth in title V of this Act, as amended*, The Secretary of Commerce may insure 100 per centum of the principal [of] and interest on any such mortgage eligible for insurance as hereinafter provided and upon such terms as the Secretary of Commerce may prescribe.

(b) The Secretary of Commerce, upon application by the borrower, is authorized to insure as hereinafter provided the interest on and 90 per centum of the unpaid balance of the principal of, any loan offered to him which is eligible for insurance as hereinafter provided and, upon such terms as the Secretary of Commerce may prescribe, is authorized to make commitments to insure any such loan prior to the date of execution or disbursement thereon: *Provided*, That in the case of special purpose vessels certified by the Secretary of Defense to be essential to national defense, *and in the case of passenger vessels having the tonnage, speed, passenger accommodations, and other characteristics set forth in title V of this Act, as amended*, the Secretary of Commerce may insure 100 per centum of the principal [of] and interest on any such loan eligible for insurance as hereinafter provided and upon such terms as the Secretary of Commerce may prescribe.